

A Reprint from *Tierra Grande*

beyond a reasonable drought

By Joe Outlaw and Charles E. Gilliland



Recently, Center staff had a conversation with noted agricultural economist Dr. Joe Outlaw concerning the state of Texas agriculture. This is a summary of his insights.

How has the drought affected Texas farmers ?

Some producers will be relatively okay because they purchased multi-peril insurance on their crops. That insurance paid off when crops failed completely. Because of changes in the price of cotton late in the 2011 season, farmers with insurance actually made more money from the payments they received than they would have made on a crop sold at prices prevailing at harvest time.

However, producers who did not buy insurance will face serious problems in repaying operating loans and negotiating loans to put in this year's crop. Lenders are going to insist that they pay something on the outstanding debt and be able to make enough to pay the new loan off.

What impact will these circumstances have on local economies in rural Texas ?

Farmers still spend a lot of money locally. In the major agricultural areas, there is an infrastructure that relies on farmers buying things such as tractors, fertilizer and seed, or hiring a flying service.

Following a drought, everyone becomes a penny pincher. That affected the 2011

crops because there was no reason to apply defoliant or fertilizer on crops that didn't come up. Those service business owners suffered last year and will face customers who are belt tightening this year as well.

What about live-stock operators ?

This is a multifaceted situation. For the first time in my memory, we've had a drought during which beef prices were pretty good. Some producers are facing high tax bills after selling mother cows for more than they paid for them because they didn't want to pay the high cost of hay. Those producers that weren't able to sell or didn't want to sell are paying more than \$100 for a round bale of hay. It is difficult to put the pencil to paper and make that money up.

Because of the sell-off, herd numbers in Texas are really low. Many acres that were taxed based on agricultural value for grazing are vacant now. To avoid paying much higher taxes, owners will have to find another qualifying agricultural use.

In addition to these issues, no one pulled the cattle off the land before it was damaged by lack of rainfall. It will take pastures years to recover and will be expensive to restock when the drought ends.

What are the latest developments in agricultural policy nationally ?

We are currently analyzing 12 potential scenarios for Congress to assist in setting up the agricultural safety net for crop producers over the next five years. The four principals on the agriculture committees

responded to the now disbanded Super Committee by agreeing to cut \$23 billion out of the ag baseline budget, with \$15 billion coming out of commodity programs over ten years. The rest will come as a \$3 billion cut from food programs and \$5 billion from conservation programs. Currently, we spend about \$80 billion on food programs, about \$6 billion on commodity programs and roughly the same on conservation programs each year. That makes the relative cut to commodity programs a big deal.

Conversations in Congress indicate that the direct, fixed payments to owners of base acres (land with eligible historic crop production enrolled in Farm Service Agency commodity programs) will probably end. That means those who bought land hoping to use that money to pay for it are out of luck. The money will be re-allocated to cover shallow losses, which are those paid by crop insurance before losses become serious.

In other words, it won't take much to trigger a payment, but the payment will be small. Texas has had deep losses, and once claimants get past shallow losses there will be no protection.

What is driving current commodity prices, and how long will that likely continue ?

Ethanol is driving commodity prices. It has been a significant driver of corn prices and that impacts everything else. It increases feed costs and influences crop decisions that in turn affect other commodity prices.

The government has mandated use of ethanol in gasoline and subsidized it with a blender's tax credit that expired at the end of 2011. Poultry, swine and

livestock producers are trying to end the mandated use as well because of ethanol's impact on corn prices, but the mandate is still in place. As a result, corn prices are likely to be high for the foreseeable future.

Is there a bubble in cropland prices ?

I do think we are in a bubble. The current farm program has supported good producer returns, and that has driven land prices up. Direct payments from that program have been capitalized into current land prices. Those are going away, and it's going to be difficult to explain the impacts when the new farm policy comes out.

Investors will have to do some serious pencil pushing to see if farmland investment is a good idea for them. The reduced safety net is going to be a lot less. This increased uncertainty is likely to make investors pause before aggressively buying cropland. ➔

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THE TAKEAWAY

Farmers, ranchers and service businesses that support them are suffering negative effects of this year's drought. To make matters worse, federal agricultural programs are on the chopping block to reduce the deficit.



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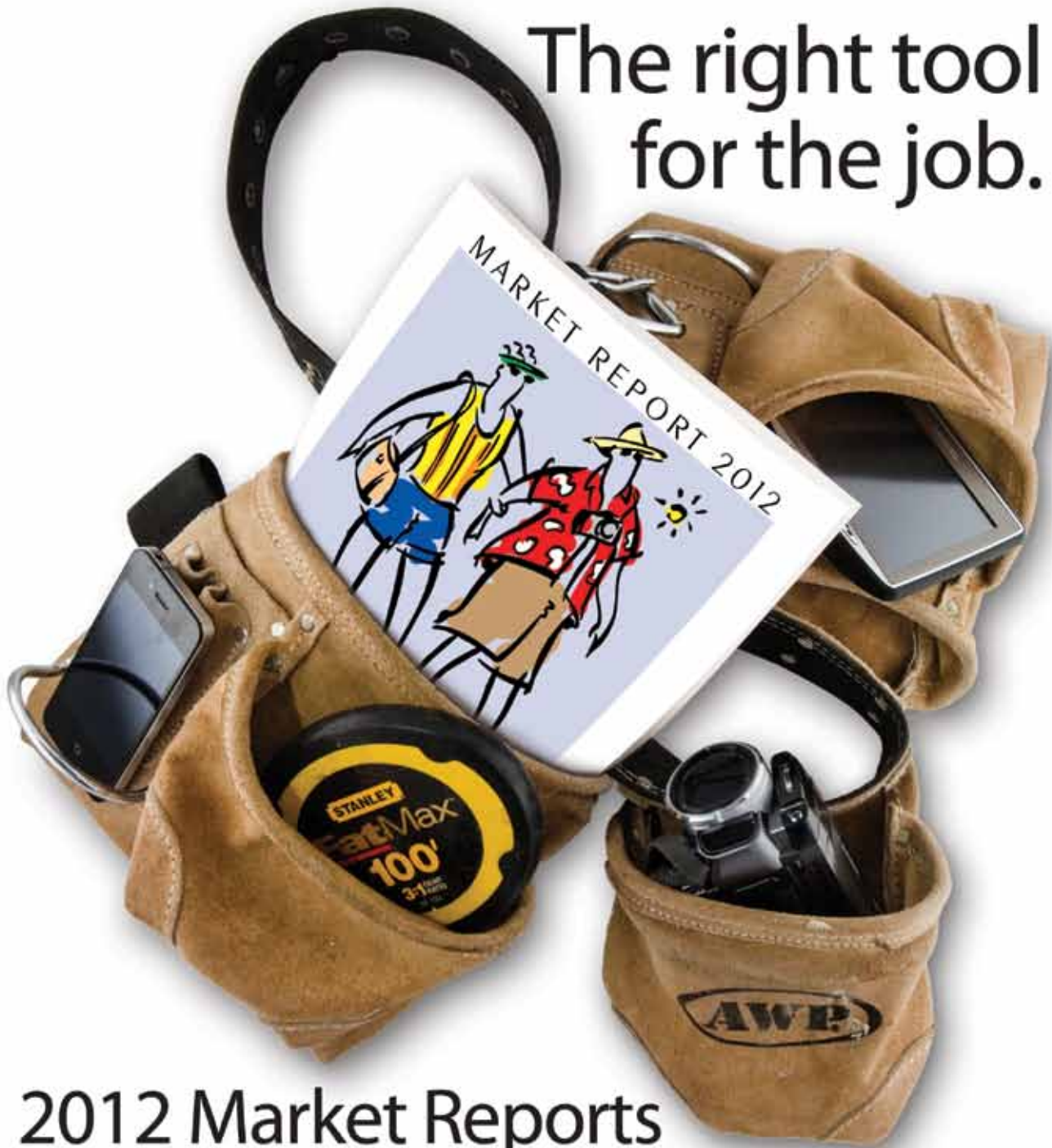
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